

Service Date: November 16, 1987

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

* * * * *

IN THE MATTER of the Montana)	UTILITY DIVISION
Public Service Commission's)	
Investigation of Federal Tax)	DOCKET NO. 86.11.62
Reform Impacts on Public)	
Utility Revenue Requirements.)	ORDER NO. 5236e

* * * * *

ORDER ON STATEMENT 87

* * * * *

1. On May 27, 1987, the Montana Public Service Commission (MPSC or Commission) issued Order No. 5236b in this Docket. Order No. 5236b set forth the Commission's concerns over the effects on operating results of Statement on Financial Accounting Standards 87, (hereinafter Statement 87), issued by the Financial Accounting Standards Board (FASB). Order No. 5236b stated: "Parties will be receiving data requests to provide the Commission with the necessary information to calculate the impact of Statement 87. In addition, all parties must file briefs addressing the following issues relating to the impact of Statement 87:

1. Does the Commission have the authority to require or deny the application of FASB Statement 87 to ratemaking, regardless of the utility's financial reporting?

2. What is the appropriate ratemaking treatment to reflect pension income, or a significant reduction in pension expense, resulting from an over funded pension plan? What is the appropriate ratemaking treatment to reflect pension expense resulting from an under funded pension plan?

3. What is the appropriate ratemaking treatment in the case of additional liability to be reported for unfunded accumulated benefit obligations and the resulting charge to an intangible asset and stockholders' equity?"

2. Initial briefs were received from the following parties: AT&T, Butte Water Company, General Telephone Company of the Northwest, Great Falls Gas Company, Montana Dakota Utilities Company, Montana Power Company, Mountain Bell, Mountain Water Company, Northwestern Telephone Systems, Inc., Pacific Power & Light Company and Montana Consumer Counsel. Reply briefs were received from Pacific Power & Light Company and Montana Consumer Counsel.

3. With respect to question #1 (Commission authority to accept or reject Statement 87 for ratemaking), Mountain Bell stated that the Commission has authority to either require or deny the application of Statement 87 for ratemaking. AT&T stated that the Commission should await the results of possible rulemaking by the FCC to consider its authority to approve or deny application of Statement 87. Northwestern Telephone Systems stated that since the Commission is not necessarily bound to follow financial reporting for ratemaking, it could deviate from Statement 87 for ratemaking.

The Company stated that the Commission should consider whether its acceptance or rejection of financial reporting methods will cause adverse consequences to customers or investors. MDU stated that Commission authority is specified in applicable Montana statutes.

MPC stated that the Commission obviously can look at the pension expense that is included in the utility's cost of service for ratemaking. PP&L commented that whether or not the Commission has jurisdiction to require or deny the application of Statement 87 in ratemaking, depends on whether application of these standards on a consistent basis will reasonably reflect the utility's actual pension expense over time. Both Butte Water and Mountain Water commented that the Commission has the authority to require the application of whatever ratemaking theories it desires regardless of whether those theories have any basis in Generally Accepted Accounting Principles (GAAP) or tax law. MCC indicated that the Commission has the authority to adopt or deny the application of Statement 87 for ratemaking purposes.

4. AT&T's proposal asking the Commission to wait to determine its authority to adopt or reject Statement 87 for the possibility of a rulemaking proceeding at the FCC is rejected by the Commission. In harmony with the majority of comments received on question #1, the Commission concludes that it does have the

authority to adopt or reject the application of Statement 87 for ratemaking purposes.

5. Next, the Commission will address the principal question, that is, should Statement 87 be adopted for ratemaking? First, a summary of comments from those parties who did not support adoption of Statement 87. While not overtly opposed to Statement 87, AT&T's comments were negative. AT&T noted that Bell South had filed a petition with the FCC questioning the appropriateness of Statement 87 for regulatory accounting. AT&T stated that funding has been used for ratemaking in the past based on the public policy criteria of 1) intergenerational equity, 2) rate stability and 3) protection of pensioner benefits. AT&T submits that nothing in Statement 87 justifies departure from these principles. The Company stated that sound actuarial methods should yield the same cumulative results in the long run. Montana Power Company seeks to continue to fund its pension plan using the method which has been used historically by its actuary. Montana Power Company believes its pension funding objectives are better met through that methodology than through the Statement 87 formula. Statement 87 will result in great volatility in the periodic pension expense. For example, for Montana Power Company the difference between 1986 pension expense calculated under Statement 87 and the 1987 pension expense under Statement 87

is over \$2,000,000. Montana Power Company stated this kind of volatility is inappropriate in a ratemaking setting.

6. Several of the parties in this Docket filed comments in favor of adoption of Statement 87 for ratemaking. Mountain Bell supported the use of Statement 87 for ratemaking because it provides more meaningful and more useful pension accounting. Mountain Bell stated that Statement 87 provides a better match of the cost of an employee's pension over the employee's service period, it is more understandable than other methods, it permits improved comparison among companies, it provides more complete disclosures and it improves reporting of financial position.

Statement 87 requires the use of one actuarial method, the "unit credit method." This method develops an increasing funding or cost pattern by assigning a larger cost to the later years of employment as the employee population ages. Northwestern Telephone Systems supports the use of Statement 87 for ratemaking because it provides a more meaningful and useful accounting of pension costs.

Northwestern Telephone Systems stated that although the pension expense under Statement 87 will increase as the employee ages, the overall effect for Northwestern Telephone Systems is not expected to fluctuate significantly because the mix of younger employees to older employees should be stable. Montana Dakota Utilities stated

that the Commission has followed the determination of pension expense for ratemaking that is determined by GAAP and, therefore, it would be improper for the Commission to deny application of Statement 87. General Telephone is convinced that the public interest would best be served by permitting the use of Statement 87 as the approximate method of calculating pension costs for ratemaking.

7. Three Companies filed comments which indicated that the provisions of Statement 87 do not apply to them. Great Falls Gas is not affected because it has a defined contribution pension plan.

Great Falls Gas stated that the Commission should concentrate on the legal requirements of reasonableness more than on the recommendations of FASB. Butte Water and Mountain Water filed identical comments. Neither company is required to use Statement 87 for financial reporting because neither has defined benefit plans with more than 100 participants. Both companies believe that pension expense for ratemaking should be based on actual pension costs paid by the utility. The Commission finds that the provisions of Statement 87 do not apply to these three companies.

Pension expense for these companies will be evaluated in future rate cases.

8. Pacific Power and Light Company does not agree that a decision on adopting Statement 87 should be made on a generic basis. PP&L's position is that it should be considered on a utility by utility basis. The Company stated that it might be appropriate for the Commission to authorize the Company to establish a balancing account for any differences between actual pension expense and Statement 87 pension expense. In its reply brief, MCC agreed with PP&L and stated that the ratemaking treatment of pension costs should be determined by the Commission on a case by case basis rather than on a generic basis.

9. Accounting for pension expense is an important issue which will impact the cost of service for regulated utilities into the foreseeable future. Just as Statement 87 represents a change in pension accounting from past methods, it is doubtlessly true that other changes in pension accounting will occur in the future. This issue generated a wide range of responses. While the responses were varied, they provided the Commission with valuable input which the Commission carefully considered in reaching its decision. In adopting Statement 87 for ratemaking, the Commission finds that use of Statement 87 will result in an improvement over past practices of accounting for pension expenses. Significant benefits of adopting Statement 87 include: comparability between companies,

recognition of pension obligations and assets, consistency from period to period within the same company and more meaningful and useful financial reports. If either a utility or MCC believes that for ratemaking, a different actuarial method would produce a more reasonable result, the Commission will consider the evidence presented to it. Such an alternative method must be provided by the parties in the context of their next general rate filing. Additionally, any utility planning to propose an alternative method must notify the Commission within 30 days of the date of this order. This provision answers the concerns of the parties who asked the Commission to address the issue on a case by case basis.

10. Adoption of Statement 87 may result in the creation of book-tax timing differences. Consistent with other decisions on timing differences in this Docket, the Commission favors the use of flow-through to account for these items. This method will be required unless the utility or MCC can demonstrate that the use of normalization will produce a more reasonable result for ratemaking.

11. With respect to question #2 in Finding of Fact No. 1, (How should the Commission treat over and under funded pension plans?) answers to this question were very general. The Commis-

sion finds merit in several points made by MPC. Determination of whether a pension plan is over or under funded could involve a substantial factual question and the proper ratemaking treatment may depend on the particular circumstances. This issue will be dealt with in future rate cases on a case by case basis. The Commission expects vigorous discussion of this question by the utilities and MCC in future rate proceedings.

12. With respect to question #3 in Finding of Fact No. 1, (What is the proper ratemaking treatment for balance sheet accounts created or determined under Statement 87?) answers to this question were again extremely general and do not constitute enough evidence for the Commission to reach an informed decision. The proper ratemaking treatment for balance sheet accounts created under Statement 87 will be dealt with in future rate cases.

CONCLUSIONS OF LAW

1. The Commission has authority to supervise, regulate and control public utilities. Section 69-3-102, MCA.

2. Respondents are public utilities subject to the Commission's jurisdiction. Section 69-3-101, MCA.

3. The Commission may regulate the mode and manner of all investigations and hearing of public utilities. Section 69-3-103, MCA.

ORDER

1. The interpretations of FASB Statement 87 set forth in the preceding sections of this Order are deemed to be generally established principles of utility rate regulation, and the existing methodology to be applied in determining utility pension expenses.

2. Great Falls Gas, Butte Water and Mountain Water are not subject to the adoption of Statement 87, since the Statement does not apply to them.

3. The revenue requirement impact of adoption of Statement 87 or an alternative actuarial method shall be reflected in the next general rate filing for each affected utility. The Commission will examine the impact of adopting Statement 87 in this Docket for Mountain Bell as testimony has been filed by Mountain Bell and Montana Consumer Counsel.

DONE AND DATED at Helena, Montana this 13th day of November, 1986, by a 4 to 0 vote.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

CLYDE JARVIS, Chairman

HOWARD L. ELLIS, Commissioner

TOM MONAHAN, Commissioner

DANNY OBERG, Commissioner

JOHN B. DRISCOLL, Commissioner

ATTEST:

Ann Purcell
Commission Secretary

(SEAL)

NOTE: Any interested party may request that the Commission reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.